

Finding India's Missing Middle



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By Kevin Conway

The middle is missing in India's labour markets and Dipak Mazumdar knows why. In truth, it was never really there, says the University of Toronto professor.

Most Indians not working in agriculture rely on the country's large "traditional" or informal sector for their livelihood, notes Mazumdar. Those employed in the country's "modern" economy work in small firms, with fewer than six employees, or in large establishments of 300 or more workers. In between is a yawning divide.

"The major reasons for India's 'missing middle' in the modern sector is the lack of development of labour-intensive industries — mid-size firms that make use of less-skilled labour," says Mazumdar.

A decade-long economic boom has done little to provide real jobs for unskilled Indians who make up the majority of the workforce, Mazumdar told delegates at a November 2006 workshop, where he presented the results of [IDRC-sponsored research in India](#) undertaken as part of a collaborative project between the University of Toronto and the Delhi-based Institute for Human Development.

The workshop, sponsored jointly by IDRC and Carleton University's Norman Patterson School of International Affairs, drew researchers from around the world to discuss the current status of global labour markets and examine how research might be used to better shape labour markets to reduce poverty and inequality.

In India's case, it will likely mean finding its missing middle.

Growth, jobs, and poverty

“Real growth and jobs have come in the tertiary sector, such as IT, and large-scale, export-oriented manufacturing,” Mazumdar says. Savvy entrepreneurs, aided by economic reforms introduced in the early 1990s, have mined new opportunities in international markets. Deftly exploiting the country’s abundant and relatively cheap pool of English-speaking college and university graduates, they have made India a destination of choice for cost-cutting companies looking to outsource services — everything from research and development to payroll and legal support. But they failed to generate the kinds of “reliable” jobs India desperately needs.

Low wage employment remains a serious problem in the Indian labour market. And yet as Mazumdar’s study on poverty, growth, and inequality shows, the number of Indians living in poverty has dropped over the past 10 years. Trade liberalization policies have played an important role, but Mazumdar also points to another reason.

“Poverty has continued to fall because of the increase in land productivity thanks largely to the Green Revolution,” he says. “But the Green Revolution needs water and fertilizer to work and there are vast areas of India which do not have water, do not have irrigation. So, the prospect of further widening the Green Revolution is limited and I don’t see where new technological breakthroughs will come.”

As the economy grows and salaries rise among the country’s highly skilled, well-educated, urban workforce, the wage gap with their rural cousins widens. Improvements in the country’s poverty picture have been tempered by rising inequality.

“Growing inequality may sow the seeds of conflict and put the brakes on poverty alleviation,” warns Mazumdar. “Furthermore, if firms are not able to respond and provide jobs to India’s huge unskilled and semi-skilled labour force, then wage costs in the industries currently driving the country’s economic boom will be a brake on further growth in the export and domestic market,” he adds.

A tangled web of legislation

A good place to start creating jobs is with India’s labour legislation, says Mazumdar. India has 45 national laws and 170 state statutes that deal directly with labour market issues. Overlapping and sometimes contradictory, they have created a tangled, complex web of inconsistently applied rules and regulations. “Even when they are not implemented rigidly, it creates a climate,” says Mazumdar.

The 1947 Industrial Disputes Act, for example, requires employers of more than 100 workers to seek state authorization before laying off any employees. Dismissals can be and usually are disputed.

“Labour courts can take months or years to settle cases,” says Mazumdar. “While large firms have well-staffed legal departments to look after this sort of thing, mid-sized firms cannot afford this kind of ‘overhead’ cost.”

A split personality

Indeed, India's manufacturing sector has a decidedly split personality. "Smaller firms specialize in the niche market of low-quality products geared to low-income consumers. Larger firms concentrate on higher quality, higher-income consumer markets including exports," says Mazumdar. Larger firms also invest in machines and technology to boost productivity rather than hire and train employees whom they may have to dismiss when the economy takes a downturn.



Dipak Mazumdar

Industrial policies rooted in the earliest days of India's independence compound the problem.

"Since the days of Nehru and Gandhi, Indian politicians have supported a dual policy," says Mazumdar. "A huge number of items for consumption were reserved for small-scale producers. Larger industrial firms had to have licenses to set up at all and by dictate they were prohibited from producing certain lines of consumer products like textiles. They remain the preserve of the small firm."

The intent of the policy was to maximize employment in the short term. The long-term result, however, is "a clear incentive to expand horizontally and not vertically," says Mazumdar. "If smaller firms were able to grow easily into mid-sized businesses, they would draw more labour from the large pool in agriculture. Incomes would rise over time and drive a mass market, which in turn would provide the necessary incentive for mass-market manufacturing."

With minor variations, this is the tried and true formula by which all of India's East Asian neighbours have climbed out of poverty.

Battling inertia

Blame for the lack of a labour intensive manufacturing industry does not lie solely with India's legislators. Industry must shake free of what Mazumdar calls its own "hysteresis." "It is more than just inertia," he explains. "When a system exists for a long time, it has certain effects that make it persist even after the initial cause is gone. It builds walls in people's minds. Reforms have been going on for 10 years and many regulations have been dismantled with no visible impact on the size structure of industry."

Continued economic growth and upward pressure on wages may well provide the incentive and opportunities for reluctant entrepreneurs.

Liberalization: The next steps

Legislators are also facing increasing pressure both inside and outside the country to continue to reform labour laws and take the next steps in liberalizing India's economy. Bringing India's small but politically powerful trade union lobby onside remains a significant challenge.

"Labour legislation favours only a minority of the workforce but you have to sell reform to trade unions," says Mazumdar. "Outside the formal sector there is no social protection. So labour reform is intimately tied to some form of protection or some measure of welfare legislation for the vast

majority of unemployed, underemployed, and poor people, otherwise politically I don't think it can be done.”

Legislators — national and state — will also need to invest in infrastructure and better primary education, if they hope to create the kinds of jobs that will continue to alleviate poverty and reduce inequality, says Mazumdar. Indians under the age of 15 account for more than a third of the population. As they enter the workforce, the search for India's missing middle may become a frantic one.

India's growing middle class, now numbering some 250 million people, has brought with it a growing social consciousness, says Mazumdar. Nongovernmental organizations representing women and workers in the informal sector — where most poor Indians work — are driving a grassroots movement that is gaining a political voice. Caught in the vice of voices clamouring for change, legislators in the world's largest democracy may have little choice but to embrace it.

Correcting the bias in education policies

“Education policy in India has been skewed to tertiary education,” says Professor Dipak Mazumdar. “Primary education has been badly neglected, even though India's 1947 constitution specified that it would be universal within 10 years. This has not happened.”

This may help explain the tardy development of labour-intensive industry in the modern sector, he notes. “Even in labour of low skill, working in modern industry requires a basic level of education. It imparts industrial discipline and literacy.”

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